

Message Text

LIMITED OFFICIAL USE

PAGE 01 STATE 204037

ORIGIN ARA-14

INFO OCT-01 ISO-00 SP-02 USIA-06 AID-05 EB-08 NSC-05
TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00
COME-00 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03
LAB-04 SIL-01 DODE-00 PM-05 AGRE-00 MCE-00 ACDA-07
L-03 HUD-01 INT-05 /103 R

DRAFTED BY ARA/AND:ASC FULLER/ARA/ECP:RTAYLOR

APPROVED BY ARA/AND:MR BARNEBEY

ARA:RG ARELLANO (DRAFT)

TREASURY - MR. COOPER (DRAFT)

COMMERCE/OIM - MR. LINDOW (INFO)

EXIM - MR. KINGSLEY (INFO)

DOD/ISA - COL. THOMAS (INFO)

AID/LA - MR. WEBER (INFO)

-----062545 260138Z /61

P 252335Z AUG 77

FM SECSTATE WASHDC

TO AMEMBASSY LIMA PRIORITY

LIMITED OFFICIAL USE STATE 204037

E.O. 11652: N/A

TAGS: EFIN, PE, EAID

SUBJECT: BRIEFING BY CENTRAL BANK PRESIDENT DE LA MELENA

REF: STATE 200380

SUMMARY - PERUVIAN CENTRAL BANK TEAM BRIEFED USG OFFICIALS
ON ECONOMIC STABILIZATION PROGRAM AND BROAD FISCAL, MONE-
TARY, BALANCE-OF-PAYMENTS AND EXCHANGE-RATE POLICIES.
REAFFIRMED MORATORIUM ON NEW ARMS PURCHASES. ASKED FOR
U.S. ASSISTANCE. FURTHER DATA ON STATE OF ECONOMY REQUESTED,
LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 02 STATE 204037

WHICH PERUVIANS UNDERTOOK TO PROVIDE.

1. AT INVITATION OF DEPUTY ASSISTANT SECRETARY ARELLANO,
PERUVIAN CENTRAL BANK TEAM BRIEFED DEPARTMENT AND TREASURY
OFFICERS EVENING OF AUGUST 23, AS THEY HAD DONE NY BANKS
(REFTEL). PERUVIAN SIDE CONSISTED OF CENTRAL BANK PRESIDENT
DE LA MELENA; BANCO POPULAR CHAIRMAN BROUSSET; EDUARDO

HILGERT PERA, CENTRAL BANK; RAFAEL OTERO, ECONOMIC ADVISER, COAP; WINSTON TEMPLE SEMINARIO, ALTERNATE DIRECTOR FOR PERU, IMF; AND AMBASSADOR GARCIA BEDOYA.

2. DE LA MELENA STARTED WITH OUTLINE OF PERU'S ECONOMIC STABILIZATION PROGRAM. HE STRONGLY EMPHASIZED THAT PERU HAS NEVER DEFAULTED ON ITS EXTERNAL PAYMENTS, NOR WOULD IT DO SO IN THE FUTURE. HE EXPLAINED THAT HIS DELEGATION HAD

NOT COME TO THE UNITED STATES TO MAKE FORMAL REQUESTS FOR LOANS FROM OFFICIAL AND PRIVATE SOURCES, BUT TO EXPLAIN THE POLICY MEASURES PERU HAS TAKEN AND TO OUTLINE THE OBJECTIVES OF THE GOP STRATEGY FOR ECONOMIC STABILIZATION.

3. HE SAID THAT WHEN HE ASSUMED THE PRESIDENCY OF THE CENTRAL BANK HE DISCOVERED THAT PERU'S ECONOMIC SITUATION WAS MUCH MORE DIFFICULT THAN HE HAD EXPECTED. HE DETERMINED THAT THE AUSTERITY MEASURES OF ECONOMY MINISTER PIAZZA WOULD HAVE TO BE COMPLEMENTED AND STRENGTHENED.

4. PERU'S STABILIZATION PROGRAM HAS FOUR BASIC OBJECTIVES: REDUCE INFLATION; INCREASE NET INTERNATIONAL RESERVES; RESTORE BALANCE OF PAYMENTS EQUILIBRIUM; AND PURSUE MODERATE PRICE AND INCOME POLICIES. THESE FOUR OBJECTIVES ARE TO BE ACHIEVED THROUGH THE USE OF FISCAL, MONETARY, BALANCE-OF-PAYMENTS, AND EXCHANGE-RATE POLICIES. LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 03 STATE 204037

5. FISCAL POLICY: THE BASIC OBJECTIVE OF THE GOP'S FISCAL POLICY IS TO REDUCE THE 1977 DEFICIT TO THE MAXIMUM EXTENT POSSIBLE AND TO WORK FOR CONTINUED REDUCTION OF THIS DEFICIT IN 1978. THIS IS TO BE ACCOMPLISHED THROUGH:

A. GRADUAL ELIMINATION OF ALL SUBSIDIES, LEAVING ONLY THOSE ON MILK AND COOKING OIL;

B. THE 8 CUTBACK IN GOVERNMENT EXPENDITURES THIS YEAR PLUS A FURTHER CUTBACK (TEMPLE HAD, IN EARLIER PRIVATE CONVERSATIONS, QUANTIFIED THE INCREMENTAL CUTBACK AS AROUND 8 BILLION SOLES);

C. ELIMINATION OF DEFICIT OF PUBLIC-SECTOR ENTERPRISES AS A WHOLE; AND

D. MORATORIUM ON NEW MILITARY PURCHASES.

6. REGARDING LAST ITEM, DE LA MELENA INDICATED HE HAD RECEIVED DIRECT INSTRUCTIONS FROM PRESIDENT MORALES BERMUDEZ TO INFORM BANKS THAT NO NEW ARMS PURCHASES WILL HENCEFORTH

BE MADE, INCLUDING REPLACEMENT ITEMS. AS REPORTED REFTEL, EXCEPTIONS WILL BE MADE FOR PURCHASES OF MUNITIONS AND SPARES. TEMPLE PREVIOUSLY HAD EXPLAINED TO PERU DESK THAT TEAM HAD TOLD BANKS OF MORATORIUM FOR REST OF YEAR AND THROUGH 1978 IN ORDER TO GIVE GREATER CREDIBILITY TO THE DECLARATION OF NON-PURCHASE. IN ACTUALITY, MORALES BERMUDEZ IMPOSED NO TIME-FRAME ON THE MORATORIUM.

7. MONETARY POLICY: THE GOP OBJECTIVE IN THIS FIELD IS TO

REDUCE MONETARY EXPANSION AS A MEANS OF HOLDING BACK INFLATIONARY PRESSURES. AN EXAMPLE OF A METHOD TO REDUCE MONETARY EXPANSION WAS THE RECENT INCREASE IN THE LEGAL RESERVE REQUIREMENTS BY 35 PERCENTAGE POINTS TO 81 ON LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 04 STATE 204037

DEMAND DEPOSITS AND TO 61 ON TIME AND SAVINGS DEPOSITS ON FUNDS DEPOSITED AFTER JULY 31.

8. BALANCE OF PAYMENTS POLICY: DE LA MELENA GAVE EXAMPLES OF MEASURES PERU HAS TAKEN TO RESTORE PAYMENTS EQUILIBRIUM. CENTRAL BANK TECHNICIANS HAVE PROVIDED HIM WITH TWO PROJECTIONS OF 1977 EXPORTS: PESSIMISTIC PROJECTION FORECAST OF \$250 MILLION LOSS IN RESERVES AND OPTIMISTIC PROJECTION FORECAST OF \$140 MILLION LOSS IN RESERVES. GIVEN THESE PROJECTIONS, THE GOP IMMEDIATELY TOOK MEASURES TO REDUCE IMPORTS BY \$200 MILLION FOR THE REST OF 1977 (\$100 MILLION FROM THE PUBLIC SECTOR AND \$100 MILLION FROM THE PRIVATE SECTOR). IN ORDER TO AVOID SPECULATION ON IMPORTS, THE GOVERNMENT ANNULLED ALL UNUSED PRIVATE-SECTOR IMPORT AUTHORIZATIONS ISSUED DURING THE FIRST SIX MONTHS OF THIS YEAR. DE LA MELENA BELIEVED THAT THESE POLICIES WOULD LEAD TO SHORT-TERM BALANCE OF PAYMENTS EQUILIBRIUM.

9. EXCHANGE RATE POLICY: DE LA MELENA SAID HE WAS QUESTIONED CLOSELY BY THE NEW YORK BANKS ABOUT PERU'S DECISION TO STOP MINI-DEVALUATIONS. HE CONTENDED THAT PERU IS NOT WEDDED TO A POLICY OF FIXED EXCHANGE RATES AND NEVER HAS BEEN. DE LA MELENA SAID PERU'S PROBLEM IN ESSENCE IS TO STOP THE INFLATIONARY PSYCHOLOGY WHICH THE PREVIOUS MINI-DEVALUATION POLICY HAD STARTED TO GENERATE IN PERU. BUSINESSMEN HAD COME TO EXPECT DEVALUATIONS AND HAD FACTORED THESE EXPECTATIONS INTO THEIR OPERATIONS. THE GOP POLICY IS TO STOP THESE INFLATIONARY EXPECTATIONS BY STOPPING MINI-DEVALUATIONS; SEE WHAT IS HAPPENING TO THE ECONOMY; AND THEN MOVE TO AN APPROPRIATE EXCHANGE RATE AT THE PROPER TIME. PERU'S GOAL IS TO ADOPT AN EXCHANGE POLICY WHICH AT THE SAME TIME IS FLEXIBLE AND REALISTIC.

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 05 STATE 204037

10. DE LA MELENA EXPRESSED THE BELIEF THAT THE INFLATIONARY PSYCHOLOGY OF THE SOUTHERN CONE COUNTRIES WAS PRIMARILY RESPONSIBLE FOR THE SOCIAL UNREST AND UPHEAVAL WHICH HAS OCCURRED IN THESE COUNTRIES OVER THE PAST FEW DECADES. HE SAID THAT INFLATION WAS NOT COMPATIBLE WITH ORDER AND PEACE, HAS BRED COMMUNIST EXTREMISM, AND BECOMES IN TIME AN ADDICTIVE "DRUG." HE REPEATED THAT GOAL WAS TO STOP INFLATION.

11. DE LA MELENA BELIEVES PERU NEEDS TWO THINGS TO HAVE A SUCCESSFUL POLICY: AN AUSTERE, EVEN SEVERE DOMESTIC

PROGRAM, AND THE SUPPORT OF THE IMF, WORLD BANK, AND PRIVATE BANKS. SINCE 1954, PERU HAS HAD MANY IMF STANDBY AGREEMENTS. HE ASSERTED THAT THE US TREASURY AND EXIMBANK HAVE BEEN "IMPORTANT PARTICIPANTS" IN THESE AGREEMENTS. HE EXPRESSED THE HOPE THAT PERU COULD CONTINUE TO COUNT ON THE SUPPORT IT HAS RECEIVED FROM THESE ORGANIZATIONS IN THE PAST.

12. AFTER HIS PRESENTATION, DE LA MELENA WAS ASKED WHAT CRITERIA PERU COULD USE TO DETERMINE EXCHANGE RATE MOVEMENTS. HE REPLIED THAT PERU HAD NOT YET DECIDED ON WHAT SYSTEM IT COULD USE, BUT THAT WHATEVER SYSTEM IT CHOSE WOULD BE THAT WHICH WOULD BE MOST CONVENIENT IN BOTH REACHING A MARKET EQUILIBRIUM AND IN PROMOTING EXPORTS. IN RESPONSE TO A QUESTION ON WHETHER HIS STABILIZATION PROGRAM COULD BE ACCOMPANIED BY SHORT-RUN GROWTH, HE REPLIED THAT STABILIZATION AND GROWTH CAN EXIST SIMULTANEOUSLY ONLY WITH AN EXPANSION OF EXPORTS. HE SAID, HOWEVER, HE DID NOT FORESEE GROWTH FOR PERU OVER THE NEXT TWO YEARS BECAUSE OF THE DECLINING PRICES FOR PERU'S MAJOR EXPORTS - COPPER, COFFEE, AND SUGAR. AT THE BEGINNING OF THE YEAR HIS TECHNICIANS PROJECTED 1978 EXPORTS AT 2.7 BILLION DOLLARS, BUT NOW THIS FIGURE HAD BEEN REVISED DOWNWARD TO 2.1 BILLION DOLLARS. THIS MEANS THAT

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 06 STATE 204037

1978 IMPORTS WILL PROBABLY HAVE TO BE 100 MILLION DOLLARS LESS THAN 1977 IMPORTS.

13. DE LA MELENA THEN MADE AN APPEAL FOR PL-480, CCC, EXIM AND AID CREDITS TO ALLOW A LITTLE FLEXIBILITY FOR PERU TO HAVE SOME SHORT-TERM GROWTH PROSPECTS. BROUSSET RECOMMENDED US ASSISTANCE IN A PROGRAM OF HOUSING FOR

LOW-INCOME FAMILIES, APPARENTLY INVOLVING SUBSIDIZATION OF HIGH INTEREST AND OTHER CONSTRUCTION COSTS. DE LA MELENA LATER "EXTRA-OFFICIALLY" SUGGESTED CONSIDERATION OF FINANCIAL SUPPORT (NOT OTHERWISE SPECIFIED) FROM TREASURY, STATE AND THE FEDERAL RESERVE SYSTEM.

14. CONCLUDING HIS REMARKS, DE LA MELENA SAID THAT PERU WOULD PREFER TO HAVE STABILITY WITH NO GROWTH FOR TWO YEARS, AND THEN TO START SUSTAINED GROWTH THEREAFTER, BUILDING FROM ITS STABLE BASE.

15. PERUVIANS WERE THANKED FOR THEIR BRIEFING. NO COMMITMENT WAS MADE IN RESPECT TO THE REQUESTS FOR SPECIAL ASSISTANCE. THEY WERE GIVEN, HOWEVER, A LISTING OF ECONOMIC DATA WE WOULD LIKE, WHICH THEY PROMISED TO PREPARE SHORTLY AND SUBMIT (PROBABLY THROUGH EMBASSY). DATA DESIRED IS RECORDED IN SEPTTEL. CHRISTOPHER

LIMITED OFFICIAL USE

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: CENTRAL BANK, FINANCIAL STABILITY, BANKS
Control Number: n/a
Copy: SINGLE
Sent Date: 25-Aug-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977STATE204037
Document Source: CORE
Document Unique ID: 00
Drafter: ASC FULLER/ARA/ECP:RTAYLOR
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D770308-0475
Format: TEL
From: STATE
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770821/aaaaarus.tel
Line Count: 241
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 7c8ae852-c288-dd11-92da-001cc4696bcc
Office: ORIGIN ARA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: 77 STATE 200380
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 12-Apr-2005 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 1481004
Secure: OPEN
Status: NATIVE
Subject: BRIEFING BY CENTRAL BANK PRESIDENT DE LA MELENA
TAGS: EFIN, EAID, PE, US
To: LIMA
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/7c8ae852-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009